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C O N F I D E N T I A L SECTION 01 OF 02 VIENNA 000350

SIPDIS

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TAGS: [ENRG](#) [EPET](#) [ECON](#) [PREL](#) [AU](#) [RS](#) [UP](#)

SUBJECT: RAIFFEISEN ON UKRAINE-RUSSIAN GAS DEAL

REF: VIENNA 42

Classified By: Deputy Chief of Mission Scott F. Kilner for reasons 1.5 (b) and (d)

Summary

1. (C) Raiffeisen International Bank AG (RIAG) Chairman Herbert Stepic told us January 30 that Gazprom was the "driving force" behind the RosUkrEnergo (RUE) joint venture with RIAG. RIAG, according to Stepic, has exerted little influence on pricing decisions, but rather was providing financing advice, accounting standards, and help in preparing for a planned 2007 IPO on the FTSE. Stepic confirmed that RIAG, through Centragas Holding AG, served as a trustee for unnamed beneficiaries within RUE. RIAG Legal Counsel Friedrich Sommer maintained that stringent due diligence by RIAG, as well as by the American risk consulting firm Kroll, had revealed no derogatory information or links to criminal activity. Stepic acknowledged the January 4 gas deal had become a loaded political issue, especially in the context of the Ukrainian elections. Stepic claimed, however, that the deal was a good compromise, with the net increase in gas prices not more than \$15-20, after subtracting out the increased transit fees accruing to Ukraine. RIAG documents indicate that four Gazprom board members, including Alexander Medvedev, hold positions on RUE's Coordination Committee. Stepic gave a synopsis of RIAG's business philosophy in Central and Eastern Europe, stressing that the bank believes in helping to transform transitional countries from within, rather than isolating regimes in a counterproductive manner. End Summary.

Raiffeisen's Focus on Eastern and Southeastern Europe

2. (U) During a January 30 meeting with visiting EUR/AGS Director Dan Weygandt, Department of Treasury Policy Advisor Justin Serafini and Embassy EconUnit Chief, the Chairman of Raiffeisen International Bank Holding AG (RIAG), Herbert Stepic, outlined Raiffeisen's strategic interest in expanding its presence in the former Communist bloc countries. Stepic noted that Raiffeisen had reacted quickly to new opportunities, establishing subsidiaries in the region as early as 1990. Today, RIAG enjoys a wide network in 15 Southeastern, and Central and Eastern European (SEE/CEE) countries. According to Stepic, Raiffeisen's economic philosophy stresses private entrepreneurship and a minimal role for government in economic affairs.

3. (C) With a population of only 8 million, Austria needed to seek out new markets aggressively and CEE, with a population of 320 million represented an excellent opportunity. Stepic acknowledged that Austria, with historical, geographical and cultural ties to CEE, possessed certain advantages vis-a-vis other Western countries. Stepic said that Raiffeisen tried to pursue an active role, through its business relations, in helping to promote market economics in the CEE. Along these lines, Raiffeisen believed in "change from within." Outside interference, such as sanctions, were often counterproductive, impeding change. Lukashenko, in Stepic's view, was an unsavory dictator, but it was better that some western influence remained in Belarus than to isolate the country.

RIAG's Involvement in RusUkrEnergo

4. (C) Stepic confirmed that RIAG, a 100% subsidiary of Raiffeisen Zentralbank (RZB), maintains a 50% share, through Centragas Holding AG, in RUE. The Gazprom Group, through Arosgas Holding AG, controls the other 50%. Centragas Holding acts as a trustee for beneficial investors. In a follow-up meeting with Treasury Policy Advisor Serafini and Econ Unit Chief, RIAG General Counsel Friedrich Sommer said that RIAG had undertaken a stringent due diligence review of the investors. Moreover, RIAG had contracted the U.S. risk consulting firm Kroll to conduct an independent due diligence. Sommer claimed neither review revealed derogatory information or links to criminal activity.

5. (C) According to Stepic, RIAG exerted little influence on RUE price structure decisions, including the price structure of the Russia-Ukraine deal. Gazprom was the "driving force" behind strategic policy. RIAG's role was that of an intermediary, with no active involvement in RUE's economic

and political decision-making.

16. (C) Sommer supplied us with the following information on RUE's management structure:

--The Chairman of RUE is Lars Haussmann. The two directors, Konstantin Chuychenko and Oleg Palchikov, are responsible for operational matters.

--An eight-person Coordination Committee decided strategic issues. Each shareholder (RIAG and Gazprom) nominated four members.

--Gazprom nominees on RUE's Coordination Committee include:

- Alexander Medvedev, Gazprom Board Member and Chairman of the Board of Gazexport;
- Alexander Ryazanov, Gazprom Board Member;
- Yurii Komarov, Gazprom Board Member; and
- Andrei Akimov, Chairman of the Board of Gazprombank

--RIAG nominees on RUE's Coordination Committee include:

- Wolfgang Putschek, RIAG Board Member;
- Reinhard Schmid-Grimburg, RIAG Director;
- Juergen Maderthaner, RIAG Director; and
- Anton Fischer, Deputy Department Head of RZB

--The company employees 10 people in Zug, Switzerland and operates representative offices in Turkmenistan and Ukraine.

Why the Two Sides Turned to RUE?

17. (C) Stepic said the initial impetus for the Ukraine-Russia gas deal was the continuous disagreements between the parties on a transit fee for Ukraine. Both sides realized it was necessary to enlist the help of a trusted, neutral party, i.e. Raiffeisen. Moreover, Stepic claimed a western financial institution was an attractive partner because it could provide advice on financing, implement reliable accounting standards, and prepare an IPO, scheduled for January 2007 on the FTSE. The names of the beneficial investors would become public after the IPO. However, Sommer speculated that RUE might disclose the identity of the beneficial owners after the Ukrainian elections in March.

18. (C) Stepic acknowledged that the January 4 gas agreement had become "very political," especially in Ukraine, where Tymoshenko has decided to make the gas deal the centerpiece of her campaign. Gazprom had almost certainly insisted on a six-month transit fee agreement, vice the five year agreement for prices, to use as a lever in the elections. Stepic opined that the Russian strategy to influence the Ukrainian election had actually backfired, as most Ukrainians were now clear how far Russia would go to interfere in Ukrainian affairs. Stepic defended the economic basis for the agreement, claiming it was a "good compromise" for both sides. Stepic admitted that exact calculations were difficult, but he estimated that, after subtracting out the transit fee revenues, the net price increase was no more than \$15-20 per thousand cubic meters.

McCaw